Supreme Court, U. S.
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IN THE

Supreme Court of the United States

October Term, 1975

No. 75-1221

UNITED STATES OF AMERICA,

Petitioner,

vs.

CONSUMER LIFE INSURANCE COMPANY,

Respondent.

RESPONDENT'S BRIEF IN OPPOSITION TO PETITION FOR WRIT OF CERTIORARI

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QUESTION PRESENTED

The question presented is whether the United States may disqualify Respondent as a "life insurance company" for Federal income tax purposes by attributing to Respondent unearned premium reserves on accident and health insurance policies, under circumstances in which such reserves were held by another insurance company unrelated to Respondent, subject to the terms of valid, customary reinsurance agreements, and were not included in Respondent's reserves pursuant to applicable state law.

STATEMENT OF THE CASE

Respondent generally accepts the statement of the facts as set forth in the Petition. However, Respondent differs with Petitioner in certain respects. Petitioner incorrectly states that Respondent "freely conceded . . . that it assumed the entire insurance risk under Treaty I on all credit life and credit accident and health policies . . . ." Petition at 7. Respondent has never formally made such a concession; rather, this statement seems to have been taken from a colloquy between the Trial Judge and counsel for Respondent at the Hearing on the Facts, concerning the operative features of the complex reinsurance transaction in issue. Transcript at 179-180, 182. Respondent does not make such a concession.

Second, the Petitioner refers to the Trial Judge's finding of fact that the Respondent's likelihood of loss pursuant to the subject reinsurance treaty was so remote as to be negligible. Petition at 9, n. 2. The Trial Judge did make such a finding, but the Respondent contended below that such a finding was not supported by the evidence and the Court of Claims made no such similar finding in its ultimate findings of fact.

Finally, certain of Petitioner's allegations concerning state law are based on issues such as the credibility of certain of Petitioner's witnesses, whereas in fact the Court of Claims, after reviewing the transcript of relevant testimony, was able to make no findings of fact which would support Petitioner's allegations.[1]

REASONS FOR DENYING THE WRIT

As the basis for its Petition, the Government asserts

[1] *See also* note 2 *infra*.

that a conflict exists as a result of the decisions of the Court below and certain Courts of Appeals which have considered cases similar to the instant case, and Petitioner urges the adoption of a uniform national rule. Respondent respectfully disagrees that any conflict exists, and furthermore, due to the very nature of the issues, respectfully submits that the review of this case would not result in the formulation of a uniform national rule.

There is a very clear factual distinction between the instant case and the case of *Economy Finance Corp. v. United States*, 501 F.2d 466 (7th Cir. 1974), *cert. denied*, 420 U. S. 947 (1975), a decision which Petitioner asserts is in conflict with the decision below. In *Economy*, the Court of Appeals was faced with a situation in which the stockholders of Economy (a consumer finance company) formed a family insurance agency which acted as agent for all of the insurance sold through the finance company. While the accident and health reserves were held by an unrelated insurance company pursuant to reinsurance agreements, the facts disclosed that, by agreement, these funds were reinvested in interest-bearing debentures of Economy, and the interest earned on these debentures was paid to the family-owned insurance agency as additional commissions. The Seventh Circuit emphasized the fact that the unrelated insurance company did not retain the reserves, and did not even retain the right to the return on the investment, due to the fact that the funds were returned to the finance company in the form of loans and the interest earned on the loans was paid to the family insurance agency. Thus the facts in *Economy* are significantly different from the instant facts and the basis for the decision in *Economy* could well be founded upon a

lack of economic substance whereas such facts are not present in the instant case. This distinction was pointed out by the Court of Claims in the case of *Penn Security Life Insurance Co. v. United States*, 524 F.2d 1155, 1162 (Ct.Cl. 1975), where the court stated that such circumstances "could well be understood as making that ceding company the agent of those taxpayers." Indeed, there is no indication that the Court of Claims would not have reached a similar conclusion had it been faced with similar facts. It is submitted that *Economy* does not present the conflict which Petitioner asserts.

The case of *First Railroad & Banking Co. v. United States*, 514 F.2d 675 (5th Cir. 1975) is also distinguishable on its facts; the insurer *and* the reinsurer in *First Railroad* were both wholly-owned by the parent lending institution, resulting in similarities to *Economy* and to the case of *Superior Life Insurance Co. v. United States*, 462 F.2d 945 (4th Cir. 1972).

The factual situations in *Economy, supra,* and *First Railroad, supra,* are clearly distinguishable from the present case and those cases do not present a conflict with the present case. Although the reinsurance treaties in both cases bear some similarities to the treaties entered into by Respondent, the relationships between the contracting parties in those cases could not be ignored by the courts. There were no such relationships between Respondent and the other insurance company. It would be futile to attempt to establish a uniform rule for application to clearly distinguishable facts.

Respondent respectfully submits that the resolution of the issue presented by this case and the other cases which are now being considered by this Court on Petitions for Writ of Certiorari are not susceptible to the adoption of a uniform rule. Each of these cases clearly demonstrates that the factual issues, the ownership structure, and the terms of the reinsurance treaties between the various companies all differ in substantial and material respects. The decisions of the courts below demonstrate that the results of these cases turn on the factual issues; thus, these cases are not appropriate for the application of a uniform rule of law, particularly in view of the lack of any precise definition contained in the statute itself. Furthermore, each insurance company is subject to different laws and regulations regarding insurance companies in the various states in which they have their principal offices or conduct their businesses, and the expressed intent of Congress in considering the *Life Insurance Company Income Tax Act of 1959* was *not* to impose a system of Federal regulation on insurance companies, but rather to base the scheme of taxation on the existing state regulatory practices. *See, e.g.*, Statements of Rep. Curtis, *Hearings on Life Insurance Company Tax Act before a Subcommittee of the House Comm. on Ways and Means*, 85th Cong. 2d Sess. 176 (1959).

In the instant case, the basis for the decision below concerning the issue of whether the reserves were required by law as prescribed by §801(c)(3) of the Internal Revenue Code of 1954 was the interpretation of applicable state law.[3] The court below rejected the Government's contention to the effect that state law was

[3] The Petitioner argues that Georgia and Arizona law did not require Respondent to establish a reserve for the accident and health policies at issue and states that the Court of Claims did not appear to refute the Trial Judge's analysis of the applicable state statutes. Petition at 21, n. 7. This statement is incorrect in

not consistent with Respondent's treatment of the reserves and stated that, with regard to doubtful or ambiguous statutes,

> ". . . it is generally accepted that in the absence of a court decision, the interpretation placed thereon by the regulatory body charged with enforcement thereof is compelling authority. Federal courts have applied this rule to state administrative interpretations or actions under state statutes." 524 F.2d 1167, 1176 (1975).

The court cited many authorities which clearly indicate that the principle of law quoted above is well established. Furthermore, *Economy* and *First Railroad* did not deal with this issue and, therefore, the conflict argued by the Petitioner does not exist as to this issue.

The Petitioner also argues that there are presently pending administratively 90 cases concerning this issue, involving more than $28 million of taxes, and that this issue has a great impact on the revenue. These are assumptions which cannot be substantiated by information available to Respondent. It should be noted, however, that this amount of taxes, even if correct, does not

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that these issues were argued by Respondent on brief at great length; see, for example, Plaintiff's Reply Brief at 22-24, 25, and 28-30 (May 17, 1975), wherein Respondent went to great length to point out that the testimony of the Petitioner's witnesses was not entitled to any weight. The court below obviously agreed with Respondent's contentions in stating:

> "Finally, with relation to the testimony of Mr. Sturtevant, who testified that the unearned premium reserve as reported by American Bankers and plaintiff were permitted 'unwittingly' by the Georgia insurance authorities, we have reviewed his testimony and it does not change our interpretation of the Georgia law above expressed." 524 F.2d 1167, 1178 (1975).

represent revenue lost but, by reason of the application of laws relating to the taxation of life insurance companies, represents principally tax *deferred* revenues.

The Petition for Writ of Certiorari in this case represents but another attack by the Internal Revenue Service upon the companies in the credit insurance industry, an attack which, for the most part, has not proved fruitful from the Government's point of view unless other non-insurance related issues have been present. The only cases in which the Government has succeeded have been those in which the facts clearly demonstrated common control of all of the parties, *e.g.*, *Superior*, *supra*, and *First Railroad*, *supra*, or control of the funds under question, *e.g.*, *Economy Finance*, *supra*. In other situations, such as *Commissioner v. First Security Bank*, 405 U. S. 394 (1972), *Alinco Life Insurance Company v. United States*, 373 F.2d 336 (Ct.Cl. 1967), *Penn Security*, and the instant case, the various legal theories asserted by the Government have not met with acceptance by the courts. In *First Security Bank* the Government relied on Section 482, and in *Alinco* the Government relied on Section 269, as well as the general theories of tax law; and finally in this case and in the *Penn Security* case, the Government relies on its theory of "reserves follow the risk." In addition to the Governments' position in all of these cases, the Treasury Department also attempted to persuade Congress that companies offering credit life and credit accident and health insurance, referred to by the Treasury Department as "specialty business," should be taxed differently from other companies, but Congress chose not to follow the recommendation of the Treasury Department. *See* Testimony of Hon. Fred C. Scribner, Jr., and Hon. Dan Throop

Smith, *Hearings on Life Insurance Company Tax Act before a Subcommittee of the House Comm. on Ways and Means*, 85th Cong. 2d Sess. 41 et seq. (1958). A review of the instant case by this Court would not serve the cause of justice in this area of the law. To the contrary, due to the many factual intricacies and variances between the state laws involved, such a review could possibly result in additional cases being litigated. It would seem that the Government's plea for uniformity could well be settled by its adoption of a position consistent with the cases already decided.

CONCLUSION

For the reasons stated, it is respectfully submitted that the instant case is not an appropriate one for review by this Court and the Petition for a Writ of Certiorari should be denied.

Respectfully submitted,

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